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Report of the Secretary-General

Addendum

International cooperation to accelerate sustainable development in developing countries and related domestic policies*

(Chapter 2 of Agenda 21)

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* The report was prepared by the secretariat of the United Nations Conference on Trade and Development (UNCTAD) as task manager for trade, environment and sustainable development. In preparing the report, the UNCTAD secretariat benefited from comments made by the secretariats of the World Trade Organization (WTO), the United Nations Environment Programme (UNEP), the Department for Policy Coordination and Sustainable Development of the United Nations Secretariat, and the Organisation for Economic Cooperation and Development (OECD). The report builds considerably on work undertaken by WTO, in particular its Committee on Trade and Environment, UNCTAD, UNEP, OECD and other bodies.

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INTRODUCTION

1. The present report reviews progress made in the implementation of the objectives set out in chapter 2 of Agenda 21 (International cooperation to accelerate sustainable development in developing countries and related domestic policies),[1] since the United Nations Conference on Environment and Development (UNCED) in June 1992.[2] Progress in the various programme areas of chapter II of Agenda 21 has not been even. Although some progress has been made in implementing programme area B, particularly through intergovernmental deliberations, progress in other areas has been remarkably slow. Moreover, the countries that are marginalized in trade are often those that are highly indebted and do not have inflows of foreign investment. Making trade and sustainable development mutually supportive could follow a two-pronged approach: (a) identify priorities for low-income countries and (b) identify priorities for middle-income developing countries.

I. ANALYSING AND EXAMINING SUCCESS STORIES

A. Promoting sustainable development through trade

2. Programme area A (Promoting sustainable development through trade) includes among its policy objectives: (a) promote an open, non-discriminatory and equitable multilateral trading system; (b) promote access to markets for exports of developing countries; and (c) improve the functioning of commodity markets, and achieve sound, compatible and consistent commodity policies at the national and international levels with a view to optimizing the contribution of the commodity sector to sustainable development, taking into account environmental considerations.

3. The most significant development since the United Nations Conference on Environment and Development (UNCED) as regards the trade-sustainable development nexus has been the adoption of the Uruguay Round of multilateral trade agreements. The Uruguay Round agreements represent a major step by the international community towards the creation of a securer trading environment via the construction of a more fully rules-based international trading system. At the same time, the Uruguay Round agreements achieved a significant liberalization of trade by establishing tariff reductions, the conversion of a wide range of non-tariff barriers to transparent bound tariffs, the adoption of enhanced and secure market access commitments, the application for the first time of multilateral rules and disciplines to agriculture and services, and limitations on the use of subsidies to promote domestic production and trade. The Uruguay Round agreements also established a system of multilateral trade obligations subject to a common dispute settlement mechanism that will place most countries at virtually the same level of multilateral obligation within a relatively short time.

4. The Uruguay Round agreements can be expected to be a positive force on international trade (on the demand side and consequently on the supply side as well) and on trade-limited income growth, in two major ways. First, once they are fully implemented, the Uruguay Round Agreement on Agriculture, market access

reforms in manufactured and industrial products, and the phasing out of the Multifibre Agreement in textiles trade are projected to raise global income substantially (estimates range from an increase of US$ 40 billion to one of US$ 215 billion relative to the 1992 base period gross domestic product of approximately US$ 23 trillion). East Asian and - to a much lesser extent - the Latin American developing regions are expected to benefit considerably from that income growth, which should in turn enable them to make advances in addressing issues of sustainability that are otherwise income-constrained.

5. Second, there is a wide range of potential benefits from tariff reductions and tariffication, strengthened disciplines with respect to non-tariff measures, and enhanced transparency and stability in the trade regimes. Preliminary analysis to date indicates that significant new trade opportunities are expected to open up for a wide range of agricultural commodities, including vegetable oils and fats, oilmeal, rice, wheat and maize, with corresponding income gains for the exporting developing countries. In the case of metals and minerals, the Uruguay Round agreements will improve the prospects for vertical diversification in developing countries. At the same time, the higher proportion of bound tariff rates should stimulate investment in local processing before export. All of these factors should reduce the income-constraint on the adoption of policies conducive to sustainable development.

6. It is possible, however - and the Uruguay Round agreements have recognized this - that during the reform programme leading to greater liberalization of trade in agriculture, the least developed and net food-importing developing countries may experience negative effects in terms of the availability of adequate supplies of basic foodstuffs from external sources on reasonable terms and conditions, including short-term difficulties in financing normal levels of commercial imports of basic foodstuffs. Because of the link between poverty and practices inimical to sustainable development, particularly unsustainable cultivation methods, the risk of a negative impact of the Uruguay Round agreements on the poorest and most vulnerable countries merits close attention; the World Trade Organization (WTO) and - within the United Nations system - the United Nations Conference on Trade and Development (UNCTAD) are monitoring the situation closely.

7. Other possible sources of loss in the existing benefits of developing countries arising from the Uruguay Round agreements will be the erosion of trade preferences in their favour consequent upon the general tariff reductions, as well as the shifts that may occur in Generalized System of Preferences (GSP) opportunities as a result of trade and investment diversion in favour of the constituent members of proposed, emerging or enlarging areas or groupings of free or preferential trade, or as a result of special or additional privileges accorded to those members by GSP-giving countries. Such costs and benefits, however, should not be considered separately from the potential direct and indirect benefits expected to be derived from the overall positive impact on the world economy of the conclusion and implementation of the Uruguay Round agreements. Moreover, since progress in other areas identified in Agenda 21, such as the provision of additional financial resources and access to and transfer of technology, has not been encouraging, it follows that trade liberalization and improved market access have become even more necessary as a means of generating finance for sustainable development.

B. Making trade and environment mutually supportive

8. Making trade and environment mutually supportive, inter alia, includes the following objectives: (a) to make international trade and environment policies mutually supportive in favour of sustainable development, and (b) to clarify the role of the General Agreement on Tariffs and Trade (GATT)/WTO, UNCTAD and other international organizations in dealing with trade and environment issues.

9. In the post-UNCED period, intergovernmental deliberations have been clearly guided by efforts to make trade and environment mutually supportive in the pursuit of sustainable development. However, there are diverging views on the amount of progress that has been achieved, partly because different paths can be followed to achieve sustainable development, so that priorities for specific issues related to the interface between environmental and trade policies differ from country to country, depending, inter alia, on environmental and developmental conditions. Intergovernmental deliberations at UNCTAD, WTO, and the Organisation for Economic Cooperation and Development (OECD) have stressed the importance of coordination at the national level and cooperation at the international level.

10. Perhaps the most important result of the intensive post-UNCED intergovernmental deliberations is that, despite differing priorities across countries as well as differing views on how to deal with specific trade and environment issues, it has been possible to maintain the momentum generated at UNCED and to promote increased awareness and understanding, as well as larger confidence and mutual respect between trade, environment and developmental communities.

11. Throughout the post-UNCED debate, Governments and civil society have reiterated their commitments to both trade liberalization and environmental protection. The principles contained in the Rio Declaration on Environment and Development and Agenda 21, as well as the principles of the multilateral trading system have been strongly endorsed; the international community has continued to strongly reject unilateralism and to seek multilateral cooperative approaches.

12. Furthermore, intergovernmental organizations, such as UNCTAD, have given high priority to implementing an environment/trade and development agenda, as called for in paragraph 2.22 of Agenda 21.

C. Providing adequate financial resources to developing countries

13. Two programme areas specifically identified for providing adequate financial resources to developing countries are (a) reducing external debt and (b) promoting foreign direct investment.

14. The rising trend in the external debt of developing countries has persisted since 1992, but trends in debt indicators for individual countries vary considerably. Even with rising debt stocks, countries with good economic performance and market access (as exemplified by some countries in East Asia) have seen their indicators improve. Similarly, for middle-income debtor countries in Latin America that had benefited from Brady deals, the economic

situation has also improved. In many of the highly indebted poor countries (HIPCs), however, debt burdens remain unsustainably high. With respect to the HIPCs, the endorsement by the international community of the initiative to establish a comprehensive approach to HIPC debt problems, which was launched by the World Bank and the International Monetary Fund at the meeting of the Development Committee in September 1996, marks an important advance. That initiative aims to ensure that all creditors provide sufficient relief to allow HIPCs to achieve overall external debt sustainability, thus enabling them to exit from the debt-rescheduling process and strengthen their poverty reduction programmes. Debt relief is conditional upon debtor countries establishing a good performance and policy record. Multilateral agencies and non-OECD official creditors are also expected to participate in the initiative. The Paris Club group of official creditors (mostly OECD countries) has been providing debt relief involving 67 per cent debt reduction (Naples terms) since the beginning of 1995 to a number of low-income countries. The Paris Club has now agreed to go beyond Naples terms to provide debt reduction of up to 80 per cent for countries qualifying for additional relief under the HIPC initiative.

15. During the 1990s, foreign direct investment (FDI) has come to play an increasingly important role with respect to providing developing countries with sources of long-term capital. According to the World Investment Report 1996,[3] FDI flows to developing countries in 1995 reached record levels of $100 billion. In addition, developing countries have become important outward investors, with flows reaching $47 billion in 1995. Those trends are reflective of the deepening economic ties between developed and developing countries, and of the growing importance of integrated international production networks, which hold the promise of contributing to environmental objectives insofar as the integration of economies through such networks encourages the transfer and harmonization of environmentally friendly technologies across borders. The recent installation of state-of-the-art production facilities by a number of automotive producers in Mexico is an example of such a response.

II. UNFULFILLED EXPECTATIONS

A. Promoting sustainable development through trade

16. As regards commodity trade, upon which many developing countries - particularly the poorest - remain heavily dependent, the positive (and potentially negative) impacts of the Uruguay Round Agreement on Agriculture have been mentioned above. Aside from the Uruguay Round agreements, there has been no significant breakthrough in international cooperation since 1992. Although six international commodity agreements (on cocoa, coffee, olive oil and table olives, sugar, tropical timber and wheat) have been renegotiated and have entered into force since then, and it is expected that the renegotiated International Natural Rubber Agreement will soon enter into force as well, few of those agreements contain action-oriented provisions that are directed towards improving the environmentally sustainable characteristics of production or consumption of the commodity in question. Some of the more positive developments are described below.

17. The International Agreement on Jute and Jute Products contains an objective to give due consideration to environmental aspects in the activities of the parties to the Agreement, particularly by creating awareness of the beneficial effects of the use of jute as a natural product. The International Agreement on Olive Oil and Table Olives also includes a provision for giving due consideration to environmental aspects at all stages of olive and olive oil production. Increased attention to the environmental aspects of commodity production and processing gave rise to an international seminar on the environmental aspects of coffee production and processing, which was organized by the International Coffee Organization.

18. Contributing to the process of sustainable development appears as an explicit objective of the International Tropical Timber Agreement. The objectives of the Agreement also include enhancing the capacity of members to implement a strategy for achieving the exports of tropical timber and timber products from sustainably managed sources by the year 2000; the promotion of the expansion and diversification of international trade in tropical timber from sustainable sources; the promotion of increased and further processing of tropical timber from sustainable sources in producing member countries; the encouragement of industrial tropical timber reforestation and forest management activities, as well as the rehabilitation of degraded forest land; and improving the marketing and distribution of tropical timber exports from sustainably managed sources.

19. Efforts since UNCED to enhance the developing countries' capacities to diversify their production away from heavy reliance on a handful of commodities have not attained notable success. A proposed fund for African commodity diversification failed to make progress in the General Assembly. Endeavours within UNCTAD have also made little headway, although member States have recently agreed to study particular successful experiences as a platform for improved policy-making in this area. Similarly, attempts in UNCTAD to pursue sustainability through the internalization of environmental costs and benefits into commodity prices have been unsuccessful.

B. Making trade and environment mutually supportive

20. It is widely perceived that mutual understanding between the trade, environment and development communities is still insufficient, and that a larger consensus still needs to be built on a common agenda in order to strengthen the mutual supportiveness of trade, environment and development. Insufficient progress has been made in designing and effectively implementing a wide range of positive measures. In particular, little progress has been made on initiatives that favour countries with only a marginal participation in world trade, in particular the least developed countries.

21. In a number of cases, efforts to make trade and environment mutually supportive have been hindered by lack of progress in other priorities identified in Agenda 21 that have implications for the trade and environment interface, in particular financial resources and mechanisms (chapter 33) and the transfer of environmentally sound technology, cooperation and capacity-building (chapter 34).

C. Providing adequate finance to developing countries

22. In spite of the HIPC initiative, a rapid solution to the debt problems of the poorest countries may not be in sight, given the requirement that qualifying debtor countries establish a good performance and policy record over three to six years before becoming eligible for additional relief. Even in some low-income countries that are pursuing sound policies, their low level of development - characterized by structural rigidities, weak institutions and administration, poorly functioning markets and deficiencies in skills and infrastructure - have prevented a rapid and strong response to reform efforts, which may delay the provision of relief under the initiative. Moreover, countries in which the implementation of adjustment programmes has been limited or has been hampered by civil strife, including a number of major debtors that have accumulated massive payments arrears, would not seem to be candidates for early consideration under the scheme even though they are classified as HIPCs.

23. Despite the overall positive trend with respect to international investment, a number of concerns remain. At the regional level, the marginalization of Africa with respect to FDI flows remains troubling: FDI flows to Africa remained largely stagnant in 1995 at $5 billion. Given the continent's substantial capital needs and serious environmental challenges, that trend is of particular concern. Furthermore, it is not clear whether foreign investors have contributed enough leadership with respect to fulfilling local and global environmental targets. Finally, while FDI has contributed positively to the economic stability of many developing countries, the increasing importance of international portfolio investment has raised concern about the possible negative effects that such volatile investment could have for the stability of developing economies that are exposed to such flows.

D. Encouraging economic policies conducive to sustainable development

24. There is now a consensus that sustainable development requires both Governments and firms to take the long-term perspective into their decision-making processes. There is also a consensus that policy reforms take a long time to design, implement and yield results, and that adjustment, particularly in the least developed countries, is a slow process that needs to take the long view in dealing with the structural problems of such countries. However, that consensus is not always reflected in the way in which structural adjustment programmes are implemented and funded. Indeed, those programmes and the facilities associated with them, such as structural adjustment facilities or enhanced structural adjustment facilities, have relatively short horizons: they are usually provided for one to three years and performance is assessed every six months, which tends to shorten the time horizon of policy makers, forcing them to seek quick results rather than pursue policies that yield results on a sustained basis.

25. Similarly, inadequate compensatory financing in the face of external shocks forces countries to make a swift adjustment in their balance of payments, which often necessitates, inter alia, a rapid increase in export earnings that

is sometimes attained at substantial environmental costs. Such distress exports were particularly notable among the middle-income debtors in the 1980s, when most of them were forced to accommodate not only sharp declines in commodity prices but also cutbacks in lending and mounting debt-servicing obligations. In some cases, efforts to attain a swift payments adjustment were an important reason for further downward pressures on commodity prices through the fallacy of composition effect. Similar conditions still prevail today among the HIPCs.

III. PROMISING CHANGES

A. Making trade and environment mutually supportive

26. Several Governments have taken steps, including through institutional mechanisms, to achieve greater integration of trade and environment at the national level, such as by promoting better coordination between trade and environment ministries. In a number of cases, there has been a larger involvement of non-governmental organizations.

27. Progress has also been made in improving environmental standards and management practices to address local, transboundary and global environmental problems. Such progress has been possible without conflict with the provisions of the multilateral trading system or with the implementation of trade liberalization measures agreed upon in the Uruguay Round negotiations. Similarly, unnecessary adverse impacts on trade have been largely avoided. Experience has been gained in the search for cost-effective solutions to environmental problems and in establishing closer cooperation between government and industry in environmental policy-making.

28. Governments have also taken steps to firmly include Agenda 21 follow-up activities, including in the area of trade and environment, in the work programmes of GATT/WTO, UNCTAD and other relevant international organizations.

29. In the case of GATT/WTO, the preamble to the Marrakesh Agreement Establishing the World Trade Organization includes, for the first time in the context of the multilateral trading system, reference to the objective of sustainable development and to the need to protect and preserve the environment. In addition, WTO included several references to environment within different agreements. Furthermore, the Marrakesh Ministerial Decision on Trade and Environment of April 1994 provides a mandate and terms of reference for the WTO Committee on Trade and Environment, and the Singapore Ministerial Conference directed the Committee to continue its work under its existing terms of reference.

30. Recently, the United Nations Conference on Trade and Development at its ninth session (UNCTAD IX) renewed its mandate in the field of trade, environment and development by endorsing decision 4/1 of the Commission on Sustainable Development on trade, environment and sustainable development.

31. The role of other international organizations has been clarified by their respective governing bodies. In addition, the Commission on Sustainable

Development has played an important role in promoting cooperation and complementarity in the work of WTO, UNCTAD and UNEP, and in identifying gaps.

32. With regard to the trade and environment debate, efforts have been made to achieve a balanced and integrated approach. In particular, some efforts have been made to include the development dimension. Similarly, several developing countries have taken a more proactive stance, adding to the debate a number of issues of interest to developing countries.

33. In the course of such debate, it has been possible to build larger confidence in the ability of the multilateral trading system to respond to environmental considerations and sustainable development objectives. Indeed, the WTO Committee on Trade and Environment has concluded that discussions have demonstrated that the multilateral trading system has the capacity to further integrate environmental considerations and enhance its contribution to the promotion of sustainable development without undermining its open, equitable and non-discriminatory character; implementation of the Uruguay Round agreements would represent a significant contribution in that regard.[4]

34. In addition, conceptual and empirical analyses and debate have helped to set aside some of the early and largely unsubstantiated fears that trade and environment policies might be incompatible and thus lead to inappropriate policy choices.

B. Encouraging economic policies conducive to sustainable development

35. The primary institutions of the United Nations system dealing with macroeconomic policies are the World Bank and IMF. Since UNCED, IMF has paid increasing attention to the integration of environment and macroeconomics. In addition to helping countries to achieve sustainable macroeconomic and financial stability - a precondition for sustainable development - IMF assists its members in preparing three-year policy frameworks that include environmental policies, and in cooperation with members, integrates the macroeconomic and financial implications of environmental policies into the policy dialogue. Since UNCED, IMF and the World Bank have also initiated country-specific work to help make countries aware of the feasibility of integrating macroeconomics and environmental considerations, and staff regularly report on environmental issues that arise in the course of their mission work. Both institutions stand ready to integrate environmental (and other social) issues into their policy dialogues with countries, should the national authorities so desire. IMF recently explored the scope for further action in the area of sustainable development in a publication on macroeconomics and the environment.

IV. EMERGING ISSUES

A. Promoting sustainable development through trade

36. Despite the lack of progress cited above, there has nevertheless occurred a tangible post-UNCED awakening of concerns about the relationship between economic growth and the natural environment, based on the realization that both commodity and industrial production activities affect the natural resource base. It has been recognized that changes in production patterns to make them consistent with sustainable natural resource use will be more difficult to effect if environmental costs and benefits are not taken into account in the prices of products, or if the adoption of environmentally preferable production methods is not facilitated by market-based approaches.

37. At the same time, there is concern among developing countries that the eventual introduction of environmental conditionalities in the commodity sector might place an additional burden on commodity producers and divert resources from normal development programmes. Those two related issues would appear to merit future attention, whether in the context of international commodity agreements or via other mechanisms.

B. Making trade and environment mutually supportive

38. There is a need to give a new impetus to the debate on trade, environment and development, based on an integrated and balanced approach. Sustainable development should focus on the promotion of trade and investment, building on synergies between trade liberalization, economic reform, and improved management of natural resources and the environment. There is a need to promote the involvement of the business community and civil society in the design of specific enabling measures, including through capacity-building, especially in the context of environmental practices of FDI. There is also a need to undertake further empirical analysis and data collection to support the debate.

C. Providing adequate finance to developing countries

39. In the context of the HIPC initiative, the concept and definition of debt sustainability becomes an important issue. Methodological questions apart, measurement and criteria used in debt sustainability analysis require some consideration. For example, are criteria flexible enough to take into account different debt situations, in particular the budgetary burden of debt? Moreover, in following the methodology required for debt sustainability analysis, social and human development factors should be evaluated, and consideration needs to be given to the problems that debtor countries face in practice.

40. The principal emerging issues with respect to international investment and the need for sustainable development concern (a) the incorporation of countries and regions that have not benefited from the FDI boom of the 1990s, (b) the potential positive role that transnational corporations could play in conjunction with Governments in achieving global goals on emission standards,

and (c) the continued competition among developing countries for foreign capital. With respect to the last issue, it remains the case that to date the benefits of international investment for developing countries and for sustainable development have been achieved in the context of a process of liberalization that has motivated transnational corporations to compete actively for markets in both goods and services and factors of production. Governments will therefore increasingly have to consider and weigh policies with a view to encouraging and fostering healthy competition, and will have to avoid policies that seek to attract capital at the expense of openness and competition or that seek to attract capital on the basis of lowest common denominator variables.

D. Encouraging economic policies conducive to sustainable development

41. In developing countries with a weak industrial base, a rapid and sustained rise in the levels of income depends on increasing investment, which has a very high import content. That in turn requires an initial reliance on the exploitation of natural resources for the export earnings needed to finance imports and investment. However, such exploitation can be detrimental to sustainable development if resources are non-renewable, such as minerals, or if the rate of their depletion exceeds the rate of their renewal, such as in the case of timber. The pressure on natural resources will vary among countries, but it is likely to be greater when imports are liberalized before a sound and competitive industrial export base is established.

42. Sustainable improvements in growth thus require a shift away from reliance on natural resource endowments towards a strengthening of the industrial base. Successful industrialization experiences show that that process typically begins with diversification to commodity processing and shifts to non-traditional agro-exports or resource-based industries in order to raise the industrial value-added component of production and exports. A subsequent step is to develop labour-intensive industries of relatively low technology, skill and capital intensity, followed over time by further upgrading into activities with higher technological and skill content, as profits from resource-based exports are rechannelled into new investment. If such an industrialization path can be attained, the country can reduce not only its vulnerability to external trade shocks but also its dependency on limited natural resources for the financing of imports and investment. Higher levels of investment and industrial upgrading can therefore contribute significantly to the protection of the natural resource base and to a more rational and sustainable use of primary commodities, especially timber, as well as mineral and other non-renewable resources.

43. Thus, adopting an integrated treatment of the bases of economic growth, by not only ensuring macroeconomic balance and stability but also directing attention to the industrial base and incentive structures, may do much to enhance the viability of policies that address the environmental and social aspects of sustainable development in individual countries.

E. Recommendations for future work

44. Further analysis and debate should focus on issues such as: (a) the search for positive incentives to assist developing countries in upgrading environmental standards, including those related to non-product-related process and production methods; (b) successful experience with the internalization of environmental costs in the case of specific commodities; (c) the effective promotion of access to and transfer of technology to help resolve trade and environment issues; (d) policies and measures for maximizing the role that FDI can play in supporting developing countries in their efforts to achieve the objectives of sustainable development, including in the context of multilateral environmental agreements; (e) trade and environment issues at the regional level, including in the context of regional economic and trade agreements; (f) the special conditions and needs of small and medium-sized enterprises in the trade and environment interface; and (g) the identification of innovative positive approaches to environmental measures, including in the framework of multilateral environmental agreements. Such work should give consideration to emerging trade and environment issues, for example in the context of policies in the field of climate change and the conservation of biological diversity. In addition, for the least developed and low-income countries, the possibility of targeting development aid as well as providing trade concessions for promoting sustainable development should also be explored.

Notes

[1] Report of the United Nations Conference on Environment and Development, vol. I, Resolutions Adopted by the Conference (United Nations publication, Sales No. E.93.I.8 and corrigendum), resolution 1, annex II.

[2] A more detailed analysis is contained in a report entitled "Trade and environment: concrete progress and outstanding issues", which was prepared by the UNCTAD secretariat in response to a request by the General Assembly contained in paragraph 26 of its resolution 50/95 of 20 December 1995. The UNCTAD secretariat is also preparing a paper on trade and environment for an ad hoc expert group meeting on the implementation of special measures for the least developed countries in Agenda 21, to be held in New York on 3 and 4 April 1997.

[3] United Nations publication, Sales No. 96.II.A.14.

[4] See WTO, report of the Committee on Trade and Environment, 1996 (PRESS/TE 014), 18 November 1996.